August 2004

Reason

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POLICY STUDY 323

Reason Foundation

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Executive Summary

Monterey County is in the process of updating its General Plan. The old proposed General Plan Update (GPU) had a number of problems and was voted down by the Board of Supervisors in May 2004. Now that Monterey County has an opportunity to draft a new General Plan Update, it can learn from the mistakes in previous work.

This report analyzes the old proposed General Plan Update and the Economic Impact Analysis (EIA) conducted by Applied Development Economics, Inc. We find that the economic analysis for the county is based on false premises and faulty economic logic. The future General Plan Update should seek to avoid the mistakes in the old proposed GPU and the EIA.

The old proposed GPU included numerous regulations that would have severely affected the livelihood of Monterey citizens. Among the documents' stated goals were the reduction of residential development and the promotion of affordable housing. Unfortunately, these goals are contradictory. By mandating large minimum lot sizes and requiring developers to provide a certain amount of money-losing "affordable housing" units, the county would only reduce the available supply of housing. This would lead to price *increases*, quite the opposite of more affordable housing.

In addition, the GPU and the EIA made unrealistic assumptions about the cost of additional services and infrastructure required by new development, particularly in rural areas. Such rural areas currently do not receive full government services. Thus, including the cost of full government services in rural development impact projections is disingenuous. Those projects that require additional services in rural areas should

instead be encouraged to ensure that developers provide the necessary infrastructure in their new developments or to form homeowners' associations or other voluntary cooperative organizations to adequately address the homeowners' needs.

The preservation of agricultural land is also a major issue. While supporters of the old proposed GPU and the EIA claim that the policies they advocate will aid farmers, the truth is that restrictive land-use regulations will only reduce the value of the farmer's chief asset: his land. Scientific and technological advances have increased agricultural productivity. Farmers should have the flexibility to use their property as they see fit and the ability to make their own land-use decisions to improve their well-being. The old proposed GPU attempted to micromanage the economy of Monterey, and it would have led to dire consequences. In every case, the old GPU and EIA call for additional land-use regulations that would have only led to greater economic hardship and a diminished quality of life for Monterey County residents. The new General Plan Update should seek to avoid these mistakes.

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Part I

Introduction

The Monterey County Planning Commission and Board of Supervisors are currently considering changes to an updated version of the county's General Plan. On June 24, 2003, the Monterey County Board of Supervisors established the General Plan Update Refinement Group, comprised of representatives of agriculture, business, community, and labor organizations, to consider and offer recommendations on the GPU. Internal disagreement and inability to reach consensus (some members have been accused of inflexibility and outright obstruction) led the Board of Supervisors to terminate the committee on September 16, 2003, although some members have since continued to meet regularly. On May 18, 2004 the Board of Supervisors voted 3-2 to delay consideration of the GPU. Citing community division over the planning document, the Board of Supervisors has directed county officials to consider alternative approaches. The process of drafting the General Plan Update is to begin anew.

Officials have an opportunity to learn from the mistakes in the old proposed GPU. The future GPU should be based on more sound economic policies and should not rely on the problematic economic impact analysis conducted by Applied Development Economics, Inc. of Berkeley. This report highlights some of the flaws in the economic analysis in those documents so that future policymakers will be able to avoid those mistakes.

The old General Plan Update (GPU) resulted from a five-year effort to revise the current General Plan, adopted in 1982, along with numerous Area Plans and Local Coastal Program land-use plans adopted during the 1980s. According to the County:

> *The Monterey County General Plan is the local constitution governing the manner in which future development will take place and the County's abundant resources will be managed and protected while meeting the needs of the projected growth over the next twenty years. The Plan serves as a guide to achieving the type of physical, economic and social environment desired by the citizens of Monterey County as growth continues to take place.*[1]

In addition to the draft of the GPU, the county commissioned Applied Development Economics, Inc. to prepare an economic impact analysis (EIA). Among the EIA's recommendations are the following:

- Ensure that market-rate new development pays its way for public services and facilities;
- Encourage phasing of development to maintain a balance of jobs and housing;
- Offer incentives to encourage below-market rate and workforce housing so that the workforce has a chance to gain a more solid financial and social footing;
- Invest in economic development to gain a greater range of employment opportunities and higher paying jobs; and

- Support basic education and workforce training to ensure a ready labor force for new business, as well as to raise the economic level of the existing labor force.[2]

The original planning principles established in the plan for Monterey County are summarized as follows:

The 1979 Growth Management Policy Established the Following Planning Principles

- Managed growth and orderly development are essential to proper utilization of land in Monterey County.
- The unique characteristics of the county's diverse regions need to be recognized in planning for growth.
- Growth must be planned only where there is provision for adequate public services and infrastructure.
- Urban growth should occur within cities and city growth areas, except where new areas of development concentration are designated by the County.
- Premature and unnecessary conversion of areas outside cities and city growth areas should be discouraged and densities should be low.
- New areas of development concentration may be designated to the extent that it better achieves the goals of farmland preservation and natural resource conservation.
- A goal of the county is to develop a proportionate share of affordable housing for low and moderate-income families. To achieve this, higher residential densities in urban areas are needed.
- Development applications should receive careful review to ensure General Plan consistency.
- Agriculture continues to be the basis of the county's economy, and productive farmland must be preserved due to its extraordinary high resource value. Development within and adjacent to productive farmlands must be nonpolluting and non otherwise detrimental to agricultural uses.
- The first priority for accommodating growth will be to infill within existing urban areas, then to develop areas immediately adjacent to urban areas where adequate services can be provided and where prime farmlands are not converted.

Source: 21st Century Monterey County General Plan Public Review Draft, January 2004, p. 7, http://www.co.monterey.ca.us/gpu/Reports/0104/0104gpu_chapter1.pdf.

The EIA focuses on the effects that new development and the General Plan Update will have on housing affordability, local government finances, and businesses, particularly the agricultural industry. The EIA accurately highlights many potential problems for Monterey County. However, neither economic theory nor historical experience can justify the EIA's proposed solutions for these problems.

The EIA fits the partisan agendas of groups such as LandWatch Monterey County, but it does not fit the needs of the rest of the community. LandWatch Executive Director Gary Patton has written that, based on the EIA's findings, the GPU must:

- Slow down growth;
- Stop low-density suburban development and focus growth in existing urban areas;
- Tie new residential development to local job growth;
- Disallow development before needed infrastructure is available;
- Require a significant share of permanently affordable housing ($376,000 and below);

- Refuse calls for the kind of “flexibility” that will undermine our agricultural economy; and
- Disallow Rancho San Juan.[3]

Unfortunately, the EIA has some serious problems. Despite the good intentions of many of the people working on the old proposed GPU, many of the conclusions in the EIA are misguided. The EIA has a number of false premises, and its authors fail to grasp some important economic principles, which leads them to questionable conclusions. The EIA seriously overestimated the amount of public services required for rural development and therefore made a misguided case for adding restrictions on rural development. If Monterey County had enacted the old proposed plan, it would have produced a number of unintended consequences harmful to the county's economy. Many of the policies would have exacerbated problems such as housing affordability rather than alleviating them. Before amending the General Plan as previously proposed, policymakers should consider the ways in which the old proposed GPU would have harmed Monterey County residents and should recognize superior solutions.

Without understanding the underlying economic causes of the problems highlighted in the EIA, one can easily advocate solutions that will make the problems worse. Unfortunately, many of the problems are caused by policies restricting development. For example, existing land-use regulations inhibit builders from providing additional housing that consumers need, which is a major cause of the affordable housing problem. Policies to further limit development will only make housing less affordable. The unintended consequence of placing restrictions on development is that fewer homes will be available, thus driving up housing prices.

In theory, new development could place a strain on county government finances when the cost of providing services is greater than the revenue generated by development. But if the county does not actually spend significant resources to serve new development, then this is not an issue. Getting an accurate picture of how much of a burden new housing actually imposes will inform sound decisions regarding development, rather than prohibiting or curtailing development for its own sake without a logical basis in fact.

In addition to containing policies harmful to the housing sector, the old proposed GPU espoused policies that would have had harmful effects on the economy. In an effort to preserve jobs, the old proposed GPU would have instead driven jobs away, which would hurt working families and businesses alike. Policies attempting to freeze the existing structure of business and industry will only harm Monterey County’s economic growth and quality of life for most residents.

As everywhere, the agricultural industry will evolve as Monterey County grows. But this change will be positive for the local economy, not negative, as some claim the EIA proves. The agriculture industry needs flexibility to improve its processing techniques, but the old proposed GPU would have severely limited this. Regulation after regulation will not help business, will not help workers, and will not help residents.

In the following analysis we look at some of the potential problems the EIA identifies for Monterey County. We specifically concentrate on improving housing affordability, allowing residential and business development without burdening county government finances, and analyzing the impact of change on the agricultural industry. Contrary to the EIA, we believe that new development does not require large public outlays as the report assumes. Rather than hurting the economy, we believe that allowing additional development would actually help the economy by making housing more affordable, creating additional jobs, and bringing additional revenue to the government.

The Affordable Housing Contradiction

Making housing in Monterey County more affordable is an important and laudable goal. The EIA estimates that 85 percent of workers in Monterey County need housing priced at $376,000 or less, yet notes that 50 percent of homes sell for nearly $400,000.[4] We agree that something should be done to make housing more affordable. The real question is how to do it. Economic theory tells us that the policies in the proposed GPU will actually make housing less affordable. By restricting the amount of housing, prices will be bid up, and low-income families will be further pushed out.

1. Restricting the Supply of Residential Land Will Make Housing Less Affordable

A central contradiction in the county's proposed land-use policy is the desire both to limit residential development—particularly low-density residential development—and increase the supply of affordable housing. By limiting the amount of land available for development (i.e., limiting the available supply of housing), the county is effectively creating a shortage of housing. This drives housing prices upward significantly. The more the housing supply is restricted, the higher prices go. Why? Imagine what would happen to housing prices if Monterey County only contained ten homes. The richest families would have a bidding war to purchase those ten homes. Now suppose the number of existing homes were to double. The richest people would still bid for the most expensive homes, but a number of homes would be available for people with lower incomes.

All economists would agree: as restrictions take more land away from residential use, the

Why Are Area Housing Prices So High?

Some sophisticated economics papers have the answer to why housing prices in California are so high. Restriction on development is one main reason. Harvard and Wharton Professors Edward Glaeser and Joseph Gyourko studied nationwide home prices and found that an "affordability crisis" only occurs in particular geographic areas with restrictive land-use regulations. The authors found that "Zoning and other land-use controls are…responsible for high prices where we see them."[*] Entitled land has such high prices because permits to build are so scarce. Glaeser and Gyourko estimate that only 10 percent of the gap between construction costs and home prices is caused by intrinsically high land prices; the other 90 percent is caused by zoning and land-use regulations. They conclude:

If policy advocates are interested in reducing housing costs, they would do well to start with zoning reform. Building small numbers of subsidized housing units is likely to have a trivial impact on average housing prices, even if well-targeted toward deserving poor households. However, reducing the implied zoning tax on new construction could well have a massive impact on housing prices.[*]

Other studies of Northern California have reported similar findings. A study by University of California, Berkeley, economists Lawrence Katz and Kenneth Rosen on the effect of land-use regulations on housing prices found that until 1970 California housing had been in line with the national average of housing prices, but by 1980 California housing prices had more than doubled the national average. They determined that one major cause of the price increase was "a massive increase in the use of land-use and growth-management techniques to slow and stop new housing production."[*] In his study of housing costs throughout the United States, William Tucker concludes, "One thing is obvious: stringent housing regulations have certainly not helped the San Francisco area solve its housing problems. They may even be creating the problems."[*]

Another study with a different methodology reached similar conclusions. Stephen Malpezzi of University of Wisconsin constructed an index of seven land-use regulatory variables and ranked 56 metropolitan areas according to how strictly they regulated land use.[*] Regulatory variables included measures such as changes in the length of approval time, time required to get land rezoned, amount of acreage zoned for residential development, and percent of zoning changes approved. Malpezzi found that a change from a lightly-regulated environment to a heavily-regulated one decreased the number of permits to build by 42 percent and increased home prices by 51 percent. Home ownership rates also declined about 10 percent. Evidence shows that areas with high levels of regulation have higher housing prices, higher rents, and lower home ownership rates.

more expensive residential land will become. The EIA misses this basic but very important point. Even though not one person at Applied Development Economics, Inc., has any graduate training in economics, they should not make this fundamental error. The two stated conclusions drawn from the EIA are inherently contradictory. Advocates simultaneously want to make housing more affordable while placing additional restrictions and limitations on new development.[5] These restrictive land-use policies will hurt the poor, renters, and young people the most. These groups are the ones that planning commissions typically claim they most want to help. As Peter Gordon and Harry P. Richardson, both of the University of Southern California, have noted, such affordable housing mandates and restrictive smart growth policies "exacerbate the problem of workplace inaccessibility by increasing housing costs for the poor, making it difficult for them to locate near areas that are growing economically."[6]

2. Imposing Price Controls on a Percentage of New Development Would Discourage Building and Make Housing Less Affordable

Another policy promoted in the EIA is equally problematic. In an effort to promote more affordable housing, the EIA advocates placing price controls on a percentage of new homes. Other names for this practice include "affordable housing mandates" and

A July 11, 2004 editorial from the Monterey County Herald *shows the problems created by restricting the production of housing in Monterey. We could not agree more. The situation is a tragedy. The solution to the lack of housing is to encourage more housing, not discourage it as the old proposed GPU would have done.*

The Herald's View: Affordable housing is a health issue

When the California Institute for Rural Studies examined the health of agriculture workers in six areas of California, researchers found many common ties. Low wages. Lack of health insurance. Poor dental health. Widespread diabetes.

However, they found that the circumstances of agriculture workers in Salinas Valley are exceptional in this respect: They have the worst living conditions. Housing "is one of the most severe and intractable issues affecting the health and well-being of farmworkers in the Salinas Valley. Housing is in short supply, terribly expensive, and often dilapidated and dangerous."

A key difference between Salinas Valley and other farming areas is the scarcity of mobile homes and trailers—just 2.8 percent of farmworkers live in them.

About 55 percent of farmworkers live in apartments, but they're often extremely crowded and in poor condition. A farmworker in a labor camp outside Soledad described a typical living arrangement: "Our little apartment has two rooms, a bathroom and a kitchen. There are nine of us living there. I sleep on a pull-down bed in the kitchen."

The shortage of available rental units makes matters worse. Many people told of seeing farmworkers with children going door to door in search of garages to rent.

About 4 percent of Salinas Valley farmworkers live in motels. One provider told of renting one room to as many as 40 men.

Other people told of farmworkers living in tents, caves and even holes dug in the sides of ditches.

Here in Monterey County.

So what does housing have to do with health?

Crowded conditions create public health problems that put both farmworker families and the general public at risk.

In crowded environments, communicable diseases such as tuberculosis can spread rapidly. Putting six to eight people in a garage, or 20 people in a two-bedroom apartment, can lead to respiratory infections, hepatitis and other infectious diseases.

Poor housing also breeds social ills. To escape from the claustrophobic environment, boys take to the streets where they can fall prey to gangs and drug abuse, which is increasingly prevalent among Salinas Valley farmworkers.

The risk of child sexual abuse rises when parents rent rooms to relatives or strangers. School performance suffers because the children have no place to study.

The valuable report was sponsored by The California Endowment, a statewide health foundation that seeks to expand access to affordable, quality health care for underserved people. The message for Monterey County is unmistakable: Providing more low-cost housing, and more housing options, is essential. People's health depends upon it.

Anecdote: Planning Commission Regulations Increase Housing Costs in San Mateo

In a May 6, 2004 Townhall.com column, "No-cost decision-making," economist Thomas Sowell reports:

A man who has been trying for more than three years to get permission to build a group of six condominiums was back before the Planning Commission again to hear how they wanted to micro-manage the construction before they would let the condos be built.

Since these six units were expected to be housing senior citizens, the developer tried to arrange the layout to minimize the ability of outsiders to get inside, so as to provide some security for the people living there. That aroused the ire of a pony-tailed commissioner, who delivered a little speech about how the way to deal with crime is not to wall it out but to confront it at the source and beat it back.

Can you imagine elderly residents confronting young hoodlums and beating them back? Can you imagine enough police being around to scare criminals off? For that matter, can you imagine a middle-aged man spouting sophomoric 1960s rhetoric?

Yet the wall that was meant to provide security to people living within this little development may have to come down, so as to allow what some commissioners called "street presence" – apparently one of the fashionable notions in which you can indulge when you are spending other people's money and risking other people's safety.

Another commissioner, a soft-spoken lady, said that she just thought that the landscaping ought to be "nicer." Who could be against nicer? Only someone who wanted to know how much nicer, at what cost – ultimately at what cost to those who will be living in the condos.

If it is nice enough for those who will be living there, why are third parties to decide otherwise? If the builder thought that making the landscaping nicer would be worth the cost in terms of a higher price for the condos, nobody on the Planning Commission would have to tell him how nice to make it. But what if the potential buyers do not consider it worth what it would cost to meet the commissioner's notion of nicer?

Then there were the inevitable complaints of existing homeowners in the area that these six condos for elderly people would add to the traffic in the area and create "parking issues" when they had visitors.

It is hard to imagine how much traffic will be created by six elderly couples hot-rodding up and down the street. And since these six condos have twelve parking spaces of their own, it is hard to imagine how parking spaces on the street will be regularly swamped by crowds of revelers.

Then there was an impassioned little speech by another current resident about "privacy issues," spiced with a reference to the Constitution of the United States, which apparently guaranteed privacy, though the Founding Fathers somehow forgot to say so.

Because the condos facing his house would be two stories high, having windows from which people could see him was apparently considered a great imposition. Presumably the gentleman has shades on his own windows that could provide privacy and he did not have to do anything out in the yard that he did not want neighbors to see.

Yet the commissioners seemed to think that there were too many windows in the plans for the condos, or windows in the wrong places. That would have to be changed to get their votes.

Both the commissioners and the neighbors are in a position to impose high costs on others at no cost to themselves. Self-indulgence is virtually inevitable under these conditions.

All this self-indulgence is taking place in northern California, where "affordable housing" is a political mantra – and a practical impossibility, due precisely to blithely piling on costs to anything that the pols would deign to allow to be built.

Collective decision-making has had such a bad track record around the world that, by the end of the 20th century, even socialists and communists were turning more decisions over to the market. But apparently the word has not yet reached San Mateo.

"inclusionary zoning". These policies restrict how much sellers can charge for a portion of a new development in order to make the homes affordable to people with "very low" to "moderate" incomes. Again, despite the good intentions of those who advocate inclusionary zoning, price controls have the unintended consequence of discouraging the production of "affordable" housing. This, too, makes housing *less* affordable to the vast majority of homebuyers.

By requiring builders to sell some units for a loss, affordable housing mandates act as a tax on the rest of the development. The economic effects of a tax are widely agreed upon by all trained economists. Taxes decrease the quantity of the good traded and increase prices. Our recent study of affordable housing mandates in the San Francisco Bay area found exactly this.[7] In the year following the adoption of an affordable housing mandate, new construction fell by more than 30 percent. We estimated that this tax on new construction adds upwards of $44,000 to the price of a new home in the median San Francisco Bay area city.

In addition to making market-rate housing more expensive, price controls fail to encourage a significant number of below-market-rate units. Approximately 50 Bay Area jurisdictions currently have affordable housing mandates, yet, the average Bay Area city produces only 15 “affordable” units per year after adopting an ordinance. Compared to the vast need for affordable housing, these programs are extremely ineffective at producing a significant number of units. At current rates of production, affordable housing mandates will require 100 years to meet the Bay Area’s current five-year affordable housing need, as estimated by the Association of Bay Area Governments.

Simply put, imposing price controls through inclusionary zoning will not improve housing affordability. If the goal is to allow more people to purchase homes at lower prices, policymakers should simply reverse the policies that have caused housing prices to become so inflated in the first place. Rather than imposing inclusionary zoning, a much simpler solution would be to eliminate so-called exclusionary zoning. Exclusionary zoning is a policy that mandates large minimum lot sizes, mandates more expensive homes, and imposes a number of other restrictions that prevent builders from providing housing to low-income families.

The proposed GPU has much in common with typical “exclusionary zoning” because it would effectively prevent low-income families from purchasing homes in most of the county. In contrast, eliminating restrictive zoning ordinances and other costly regulations would allow the supply of housing to increase, and thus housing prices would fall to more “affordable” levels. Price controls are perhaps the worst way of providing affordable housing.

Part 2

Growth and the Costs of Government Services

According to the GPU and the EIA, rural development requires significant expenditures from government. Closer analysis reveals, however, that this need not be the case. If the estimates of the cost to provide services to rural areas are unrealistically high, then the proposed restrictions on development are unjustified. We believe that the GPU and EIA significantly overestimate the burden created by new housing in rural areas. Rather than being a drain on the Monterey County economy, increases in the housing stock need not cost government revenue at all. These increases will provide benefits to the community, such as bringing in jobs and creating more affordable housing in the county.

The EIA claims that residential growth is problematic because it is not revenue-neutral—that is, "all residential developments generate a negative fiscal impact on the County."[8] This has led the EIA to conclude:

- "[T]he County may wish to avoid encouraging substantial industrial development in the unincorporated area in the Central Salinas Valley or South County" (p. 7),
- "[T]he County should avoid significant amounts of low-density development in rural, poorly-served areas" (p. 22), and
- "New development may lead to further degrading of public infrastructure." (p. 63)

A 2001 study by MuniFinancial, summarized in the EIA, estimates the net fiscal impact of a dwelling unit consisting of residents who both live and work in the unincorporated county is a cost (net loss) of $74 per year. The costs are greater in cases in which residents live in the unincorporated county but work in an incorporated city within the county ($356 per residence per year) and cases in which residents live in the unincorporated county and work in another county ($466 per residence per year).[9] Even assuming these numbers are accurate, they should not be given too much weight. U.S. Census data from 2000, after most of the Silicon Valley tech boom had taken place, reveal that 89 percent of the working population of Monterey County worked within the county.[10] Moreover, despite the more general economic boom of the mid- to late-1990s, this is down only slightly from the 92 percent of residents working within the county in 1990.[11]

In addition, the MuniFinancial report asserts that "Employment-related land uses tend to be fiscally positive regardless of location (unincorporated or incorporated) because of much lower service costs compared to residential land uses."[12] Thus, the EIA stresses "the need to maintain a balance of jobs and housing in all jurisdictions."[13]

But is it necessarily true that new development in outlying areas is more costly than infill development? Does the county really need to spend significant resources to provide infrastructure and public services to new developments? Other studies, such as one analysis of development conducted at Montana State University, have concluded that rather than being a drain on local government coffers, new housing development results in a net increase in revenue.[14] For this and other reasons, we believe that the estimates in the EIA are not as scientific as they appear.

The County Overestimates the Costs of Servicing Rural Areas

The conventional wisdom of restrictive land-use advocates is that high-density developments are cheaper to develop and to provide government services to than low-density developments. The notions that development must be concentrated within cities and rural areas must be protected thus follow. The EIA assumes that the county must provide a myriad of public services to development in rural areas. In reality, the county does not provide many of the services that the report assumes are required. We discussed this issue with residents of Monterey County to get a more accurate picture than the one described by the EIA.

Consider the account given to us by one resident of Big Sur:

> *In my rural area [Big Sur], the county provides no sewers, little if any flood control, no water, little police (one part-time sheriff patrol), one or two very small county branch libraries, no medical services (local health clinic is mostly privately funded), no fire protection (two volunteer fire departments). The only service I have heard people requesting more of is police protection (business owners want a resident sheriff restored).*[15]

Rather than spending large amounts of money serving rural areas, the county spends little. In many rural areas where it would be very expensive to provide services, the county simply does not provide certain services to these citizens. By making unrealistic assumptions, such as that it is necessary to provide "full" government services to accommodate new development in rural areas, the EIA is stacking the deck against new development. Much of the justification for restrictions on development makes little sense when one realizes that rural development does not require as much spending as the EIA assumes.

In addition to overestimating the cost of services to rural development, the EIA makes a number of questionable assumptions about how revenue is generated in each area. The EIA justifies city-centered growth based largely on the assertion that the per-capita cost of providing public services to areas at rural densities is more expensive than the per-capita cost of providing public services to areas at urban densities. This is false. Public services are not paid for with a per-capita tax. Imagine if the government either had to provide fire services to one high-density building with one hundred residents or to fifty low-density homes with the same population. Even if serving 50 different homes is 50 times more expensive than a single building, it does not necessarily follow that the county will save money by mandating that residents live in the high-density building. If each person had to pay a per capita tax of $1000, the revenue generated in both developments would be the same, and one could make a case that the county would save money by mandating that residents live in the building that is cheaper to serve. If, on the other hand, each structure had to pay a tax of $1000, the 50 homes would generate 50 times more money than the one building. Of course, neither situation completely captures the nature of the tax system, but the first situation (which the EIA implicitly assumes) is much less realistic than the second.

In reality, property taxes, hotel transient occupancy taxes, sales taxes, and other sources pay for public services. Hence, property owners pay taxes based on the value of their land. Low-density housing pays taxes based on the value of that housing, so the real questions are how much does each unit cost the county and how much tax revenue does each unit generate. If a development generates additional revenue for the county, then it pays its own way for the services the county provides it. The real question is, does a given planning area pay its way for the services the county provides to it? If so, what is the problem?

We can even question the assumption that packing people into high-density developments is cheaper than allowing them to live in low-density developments. Several academic studies have found that higher-density developments are actually more costly to serve. Economist Randal O'Toole notes: "Older studies that purported to demonstrate the 'costs of sprawl'—which were based entirely on hypothetical data—seem to have gotten it backwards: An analysis of actual urban service costs by Duke University researcher Helen Ladd found that the costs are higher in higher densities."[16] The Cascade Policy Institute confirms: "High density projects are expensive for both private developers and local governments. According to a recent report by the Portland City Club, the costs of development are about $62 per square foot for densities of 0 to 20 units per acre, but rise steadily to a high cost of $126 per square foot for densities above 200 units per acre."[17] Development in Monterey will not reach 200 units per acre in the foreseeable future but the point is that higher density is more costly. A 1997 study of new housing development in the Portland, Oregon area produced similar results:[18]

Building Cost by Height and Density

Framing	Height		Density	
	# of Stories	Per SF	Units per Acre	Per SF
Wood	2 Story	$67	0-20	$62
	3 Story	$85	21-50	$81
	4-5 Story	$99	51-100	$95
Concrete	5-7 Story	$139	101-200	$104
			200+	$125

Source: William L. White, Robert Bole, and Brett Sheehan, *Affordable Housing Cost Study: An Analysis of Housing Development Costs In Portland, Oregon*, December 1997, http://www.hdc1.org/downloads/AHCS-analysis.pdf.

Gordon and Richardson also support these findings:

> *The Real Estate Research Corporation's 1974 Costs of Sprawl report used questionable simulations to make the case for infrastructure savings associated with high residential densities. Although the methodology used renders the findings highly dubious, the conclusions have been widely cited. Moreover, recent studies that attempt to rehabilitate the approach are not very convincing. Data show that (1) high-density urban areas have the higher infrastructure costs, and (2) the lowest per capita infrastructure costs are in areas with 250-1,250 people per square mile.*[19]

Finally, Harvard researchers found that it is far cheaper to provide public infrastructure to new developments than to expand infrastructure in existing areas to support the higher densities required by smart-growth policies.[20]

The above economic studies cast doubt on the conventional wisdom about the costs of development often cited in Monterey County. In addition, whatever the actual costs of low-density development versus high-density development, differing economic conditions, demographics, and personal preferences will often

render one type of development more appropriate for a particular city or county during a particular time. This will depend on both the benefits to consumers and the costs of the developments. How the government can measure all the costs and benefits is unclear.

Many Public Services Can Be Provided at the Local Level at No Cost to the County

As noted above, we believe that the GPU significantly overestimates the cost of serving residents in rural developments. But suppose for the moment that rural development must have many services that would cost much more than the revenue generated from their property taxes. Does it follow that the rural development should be restricted? The answer is no. An alternative solution would be to require residents in rural areas to provide the services for themselves. Consider, for example, the many areas that have volunteer fire departments. If developers or homeowners realize that they must incur the costs of adding infrastructure and certain collective services if they are to live in rural areas, and are willing to provide these things for themselves, the county has nothing to worry about. In this section we assume that services are costly and necessary, but we discuss how they can be provided at the local level, at no cost to the county.

In addition to arrangements such as volunteer fire departments, many public services can be provided by developments that contain homeowners' associations. These associations can be given the authority to manage and finance many of the services the county currently provides. If a builder must put in new roads, sewer lines, and other infrastructure to build a new development, the responsibility for maintaining these services can be turned over to the homeowners' association when the development is complete. Homeowners' associations can also maintain or modify any protective covenants or restrictions placed on the development. This type of development financing has two distinct advantages over county provision: (1) New development does not burden existing government finances, and (2) The decentralized nature of this system allows homeowners' associations to tailor land-use decisions to small areas rather than imposing one-size-fits-all requirements upon the entire county.

One of the most notable trends in the housing industry in recent decades has been the growth of privately-governed neighborhood associations, or "common-interest developments" (CIDs), and there is no reason Monterey County should be an exception. Researchers report:

> *Since 1970, approximately one in three new residential units built in the United States has been in a development with a community association. In the largest metropolitan areas, more than 50 percent of new home sales are in community associations, and 6000 to 8000 new community associations are formed each year.*[21]

Such a system has the potential to save government large amounts of money. As a Fannie Mae Foundation report explains:

> *Over the past 30 years, this massive privatization of local government functions, consisting of over 230,000 housing developments containing about 47 million people, or one-sixth of the U.S. population (Community Associations Institute 2002), has changed the appearance and organizational structure of the nation's urban areas.*[22]

Homeowners in such communities become members of a voluntary local government operated by their own homeowners' association. Members pay dues to maintain facilities and provide community services, including the provision and maintenance of buildings, streets, pools, and recreation centers.

The local provision of infrastructure and services is not limited to small-scale condominiums. Sea Ranch, a private development along the Northern California coast, has more than 10,000 residents. This community provides its own privately owned roads, sewers, electricity, fire protection, security patrols, hiking trails, golf, tennis, swimming, and even a private airstrip.[23] Sea Ranch also has an excellent reputation for preserving its natural environment and wildlife.

Such arrangements need not be elitist, country-club atmospheres that exclude poorer members of society. Just as different cities provide different types and qualities of services, so too will private community organizations. As with other goods and services, the market will adjust to satisfy varying types and levels of demand. Potential residents will be able to select the communities that best suit their budgets *and* quality-of-life needs.

These associations provide many of the services that the GPU and EIA assume Monterey County must provide for new development. But, there are alternatives:,

> *Privatization of water and sewer services is already well established policy nationally as well as internationally. Nationally, 509 publicly owned wastewater treatment facilities are operated by private companies and market analysts expect this market to grow 15 to 20% each year. Privately owned and operated water companies serve roughly 15% of the U. S. market, and 433 facilities are publicly owned and privately operated. Privatizing roads could be accomplished by devolving responsibility for building and maintaining roads to neighborhood associations, developers, and special taxing districts.*[24]

Although the GPU assumes that government must provide new development with new roads, this need not be the case. Historically, many private roads (even for long-distance travel) have existed.[25] In addition to privately financed roads in gated communities and shopping malls, limited-access toll roads built and operated by the private sector exist in Orange County, California and Northern Virginia. Even security services are offered in great abundance in the United States. Private security companies such as ADT protect office buildings, shopping malls, gated communities, and individual homes.

The private provision of infrastructure and community services, particularly in rural areas, would allow Monterey County to grow without burdening government finances. In addition, the system of local provision is fairer because only the people that use such infrastructure need to pay for it. When the county builds a road, all taxpayers have to foot the bill, but when a local company constructs a road, only those who drive on that road pay for it. Thus, the local provision of public infrastructure offers an alternative to county service provision that is more efficient, more responsive to the public's needs, and fairer from a financing perspective. The local provision of these services would give Monterey County the ability to allow construction without burdening the public sector.

The County May Not Be the Best Judge of What Type of Housing People Must Live In

Despite their best efforts, government planners are not the best people to decide in what type of housing Monterey County residents must live. Market conditions change over time. If the county mandates one type of development and restricts another, it may end up passing policies that are contrary to the wishes of housing consumers. As a recent study explains, "Every parcel of land has a myriad of potential uses. The task of determining the ideal use for each parcel, in jurisdictions that may be thousands of square miles, is simply too daunting. It requires more information than could ever be processed by a central body, and even

if it could be, it would quickly become outdated."[26] Thus, no formula or set of regulations can be devised to come up with this ideal.

Planners face this problem:

> *It is not too much to say that urban planning requires perfect omniscience about the future. Unlike individual or corporate planning, urban planning also requires omniscience about the needs and desires of all the current and future residents of the urban area. Urban planners have no better crystal ball for predicting the future than individuals or corporations. Nor do they have special insights into the hearts of all current, much less future, residents. Planning an individual city or suburb is an impossible job.*[27]

By placing too much decision making into the hands of the county, the likelihood that land will be used inefficiently will increase. By locking in a system of land regulations, Monterey County would severely limit the housing choices of its residents.

Part 3

Agricultural Impact

The GPU and EIA place a great deal of emphasis on the preservation of the agriculture industry. Yet the agriculture industry needs flexibility and innovation, not restrictions on their land and their way of doing business, as the county proposes. The proposed policies will have the unintended consequences of hurting farmers and destroying jobs. Let us consider why.

As expressed in both documents, the perceived need to protect the industry is based on a preference for the agriculture industry over all others coupled with the notion that flexible land-use policies lead to an erosion of agricultural land, which is seen as harmful to the agriculture sector. The EIA, quoting another recent study aimed at analyzing agricultural and land-use policies across a number of counties, advises:

> *Policies that provide more flexibility regarding use (e.g. the proposed more expansive definition of what constitutes and [sic] agricultural activity) may improve agricultural land value or farm income but in aggregate and over time weaken overall agricultural viability by increasing land values beyond the point supported by agricultural value.*[28]

Yet, the loss of agricultural land may not be the crisis it has been made out to be, and efforts to preserve the land may end up hurting those responsible for the health of the industry—the farmers.

Agriculture is unarguably the dominant industry in Monterey County. According to the EIA,

> *This industry produces some $2.9 billion in sales of agricultural commodities in Monterey County, and supports an additional $2.3 billion in economic output from related businesses. This $5.2 billion in total economic activity supports more than 66,000 jobs, or 40 percent of total employment in the county, not including additional employment associated with food processing industries.*[29]

As impressive as the standing of the agricultural sector in the county is, this does not mean that elected officials and planners should be regulating it in an effort to save it. Such regulations would have adverse effects and would limit the ability of businesses to create new jobs.

The Proposed Land Restrictions Would Hurt Farmers

If the goal is to help farmers, the county should *not* pass policies that will hurt those very same people. However, the restrictions outlined in the proposed general plan will do just that. The farmer's main asset is the valuable land in which he has invested. By imposing restrictions on how farmers may use their land, the GPU would eliminate much of that value. Farming is not an easy way of making a living. When the sector

is not doing well, one way farmers can prevent personal disaster is to sell part of their land for non-agricultural use or to other small farmers. This acts as insurance for the farmers and enables them to profit from their years of investment in the land.

Furthermore, increases in agricultural productivity have rendered some farmland superfluous so it can be freed up for more productive uses. This can include processing facilities or other needs that will enable farmers to remain competitive. Now farmers can produce the same (or greater) output as in the past on less land, so reductions in the amount of agricultural land would not mean a loss of jobs or agricultural output. In fact,

> *…over the past five decades, the development of better plant varieties and animal breeds, and the production and better use of herbicides, pesticides, fertilizers, and other agronomic technologies—collectively known as the "Green Revolution"—dramatically increased per-acre agricultural yields. That is perhaps the most remarkable environmental success story in history.*
>
> *From 1961 to 1993, the earth's population increased 80 percent, but cropland increased only eight percent, all while per capita food supplies rose. Higher food demand was met almost totally by increasing per-acre yields. Had that not been the case and agricultural productivity in 1993 remained at the 1961 level, producing the same amount of food would have required increasing the amount of cropland and grazing land by 80 percent or more.*[30]

If this increase in productivity has taken place on a global scale, it has certainly taken place in the third most productive farm county in the United States.[31] Indeed, even the EIA recognizes that less agricultural land may be needed as in the past. According to the report, "the [agriculture] industry is constantly achieving higher productivity rates on existing land, which leads to greater production on less land. Also, high value crops such as vineyards are expanding in the southern part of the county on previously less valuable land, driving up the total production value of crops in the county."[32] These productivity gains have given farmers an opportunity to offset increasing costs such as water and labor (particularly workers' compensation costs, which have hit the agriculture industry just as hard as other industries in California) by selling land to others. Given the valuable climate and soil conditions that make the county a prime spot for farming, those who do sell land will likely end up selling it to other farmers, but they should not be prohibited from selling to non-farmers if a reasonable opportunity arises.

Although the proposed GPU intends to help farmers, agricultural "land preservation" policies actually do great harm to farmers, who are also property owners. When exclusive agricultural-use or large-lot zoning restricts a land's use, the value of that land decreases. In fact, "attempts to directly control and regulate land use through specialized agricultural zoning or comprehensive planning is likely to harm farmers. Preventing future development through public policy runs the risk of reducing the market value of farmland and thus eroding the value of a farmer's chief asset."[33]

Farmers who sell their land do so for a reason. Some commentators behave as though farmland is disappearing without cause, but the reason is straightforward. When land is transferred, it benefits farmers and non-farmers alike. A farmer may sell some or all of his land because he wants to trade land for something more valuable. The farmer is clearly better off when he sells land, but what about the rest of us?

Some have argued that the loss of agricultural land will impose economic hardship on Monterey County because of the loss of jobs. These fears are unfounded. As agricultural land is converted to other uses,

particular agricultural jobs will be lost, but other jobs in different industries will be created. In fact, the EIA even notes that its own estimates show that job creation will more than offset any agricultural job losses.[34] People who claim that the conversion of agricultural land will, on net, harm the Monterey County economy have absolutely no economic basis for such a claim.

The EIA spends a lot of time discussing the need to save farming jobs. But one must realize that as government increasingly "protects" one type of job, the region will realize fewer jobs of other types. Many attribute the high unemployment in Europe to policies that "protect" old jobs but unintentionally inhibit the creation of new ones. For every job saved in the farming sector, chances are that one (or more) new job is not created because of the protectionist policy. Hospitality, retail, high-tech, and other significant sectors of the county's economy will have fewer resources available, and workers will be stuck in less productive jobs. Are county planners the appropriate people to decide the future course of industry?

Analysis: Farmers Prefer to Make Their Own Land-Use Decisions

In the report "Urban Sprawl and the Michigan Landscape: A Market- Oriented Approach," (Mackinac Center for Public Policy, October 1998, p. 48) Samuel Staley describes how agricultural land-use policies hurt farmers:

A prime example of how well intended programs may not achieve intended outcomes is Michigan's Farmland and Open Space Program, which aims to preserve farmland by allowing farmers to voluntarily withdraw their land for future development in exchange for tax credits. The program, which was initiated in 1974 by Public Act 116 and amended in 1996, now enrolls 41% of the state's farmland.

The counties facing the most pressure for development are the central city counties and the surrounding suburban, or "collar" counties. Yet, some of the counties with the highest amount of land enrolled are rural. Of the 13 counties with more than 100,000 acres in the program, nine (62.9%) are counties outside of metropolitan areas and face little development pressure.

Since urbanized counties have lost substantial portions of farmland to urbanization, of course, significant amounts of acreage might not qualify for the program, biasing enrollment numbers toward rural counties. A quick look at other central city and collar counties, however, shows that several have more than 100,000 acres of farmland, including the counties housing some of the state's largest cities — Ann Arbor, Flint, and Grand Rapids. Some of the smallest proportions of land in the program are in the suburban Detroit area. All of these central city and collar counties have less than half their farmland in the program.

This undermines the notion that farmers and rural property owners are universally in favor of protecting farmland from development. If farmland owners were interested in protecting their land from development, they would naturally enroll their land in the program to secure the tax credits and other exemptions. The fact that farmers and property owners in central city and collar counties are not enrolling their land in the program suggests they prefer to leave their development options open for the future.

This is a strong argument in favor of economic policy neutrality for the state of Michigan.

Farming provides many jobs today, and given the stability in the amount of agricultural land in the county over the past several decades, it will likely remain the county's dominant industry for the foreseeable future. But this need not always be the case. At one point in history, most Americans were farmers. Should we expect this to be the case forever? Standards of living would surely be lower today if the United States had

adopted policies to preserve the agricultural industry's structure as it existed in 1900. In fact, many successful communities were predominantly agricultural areas not so long ago. These areas have since developed and achieved an even higher standard of living. As the economy changes, the relative value of land (and its varying and potential uses) must be allowed to change with it. Attempts to “preserve” the current structure of the agricultural industry in Monterey County only promote inefficient land use and force farmers to remain in jobs that they do not want to do.

As science and technology improve the agricultural sector and not as much farmland will be needed for production, it makes little sense to keep land for farming that would be more valuable for housing. In short, it would be inefficient to preserve unneeded land that could be better used elsewhere. Yet, the old proposed GPU would have prevented land from being upgraded by farmers or converted to residential use when other needs, such as the need for housing, are strikingly clear. Imagine a farmer who cannot compete in the marketplace because of onerous regulations imposed by Monterey County. Not only would he be unable to make a profit, he would be forced to hold onto his losing business or lease his land at a significant loss. This hardly seems to be a policy that would help industry or farming families in Monterey.

Part 4

Conclusions

Officials have an opportunity to learn from the mistakes of the Economic Impact Analysis. The same errors should not be made in the future General Plan Update. The Economic Impact Analysis of Monterey County's General Plan Update highlighted two important problems: housing affordability and the fiscal burden on local governments caused by new development. However, the conclusions that development needs to be limited and guided to particular areas while below-market rate housing is mandated are not justified by these problems. In fact, the "solution" of limiting development directly contradicts the housing affordability goal. Land-use regulations that limit development drive up housing costs and hurt the poor. Affordable housing mandates are incapable of solving the housing affordability problem and actually make it worse for the vast majority of homebuyers.

One policy that is compatible with making housing more affordable, while not burdening local government finances, is to allow all development that is willing to provide its own infrastructure and services. The private provision of infrastructure and services through homeowners' associations and other private arrangements has a long and successful history. Allowing all development that will provide its own services will increase the stock of housing and improve home affordability without negatively affecting government finances.

Greater development will cause some agricultural land to be converted to other uses, but this is not bad for the economy. Only land that is more valuable in other uses will be converted. High-value farm production is unlikely to be eliminated because this would be the most costly land to convert to other uses. On net, jobs will not be destroyed by the conversion of some agricultural land. By allowing the market to determine the optimal mix of land use, a more efficient pattern of jobs and residences will emerge, one that will raise living standards and employment in Monterey County. Most farmers would benefit from such a policy. The land a farmer owns is often his greatest asset. Land-use regulations that prevent farmers from converting land to other uses destroy the value of the land to both the farmer and the community as a whole.

Monterey County is at an important stage of its General Plan Update. If the county adopts policies that restrict land use and limit new construction, the housing affordability crisis will worsen and economic development will be limited. If, instead, self-financing development is permitted, optimal land use patterns will spontaneously emerge, housing affordability will improve, and the standard of living for Monterey County residents will rise.

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Supply and Affordability: Do Affordable Housing Mandates Work?, by Benjamin Powell and Edward Stringham, Reason Foundation Policy Study No. 318, April 2004, http://www.rppi.org/ps318.pdf

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[1] 21st Century Monterey County General Plan Public Review Draft, January 2004, p. 3, http://www.co.monterey.ca.us/gpu/Reports/0104/.

[2] *Monterey County General Plan Update: Economic Impact Analysis* (EIA), Prepared by Applied Development Economics for Monterey County, February 2004, p. vii, http://www.co.monterey.ca.us/gpu/news/ADE%20Econ%20Report%20022704.pdf.

[3] "LandWatch Comments on the Economy, Jobs and Housing," LandWatch Monterey County, open letter to the Monterey County Planning Commission, March 15, 2004, http://www.landwatch.org/pages/issuesactions/countyplan/031604jobs.html.

[4] EIA, pp. v-vi.

[5] Some advocates of growth controls contend that their policies do not increase housing prices because "demand" determines prices. This is completely false. The most basic lesson of "Economics 101" is that it is the interaction of supply and demand that sets prices. Growth controls decrease supply and increase prices. All economic theory and empirical evidence demonstrate this fact. Accounts such as "Housing Prices and Growth Management" (http://www.landwatch.org/pages/issuesactions/housing/052202prices.html) are completely ignorant of the most basic economic theory and lack any consideration of the overwhelming evidence.

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[16] Randal O'Toole, "The Folly of 'Smart Growth,'" *Regulation*, Vol. 24, No. 3, Fall 2001, p. 25, http://www.cato.org/pubs/regulation/regv24n3/otoole.pdf, citing Helen Ladd, "Population Growth, Density, and the Costs of Providing Public Services," *Urban Studies*, Vol. 29, No. 2.

[17] John A. Charles, "The incredibly shrinking roadway system: Portland's campaign against the automobile," Policy Perspective No. 1015 (Portland, OR: Cascade Policy Institute, July 2000), http://www.cascadepolicy.org/..%5Cpdf%5Cenv%5CP_1015.htm.

[18] While Monterey County is not likely to see anything like the population density of Portland, Oregon, in the foreseeable future, the numbers are nonetheless instructive. Proposals to increase population densities in urban areas, such as that contained in the proposed GPU, will only result in higher costs of development (and thus higher prices) in those urban areas, making this urban housing less—not more—affordable.

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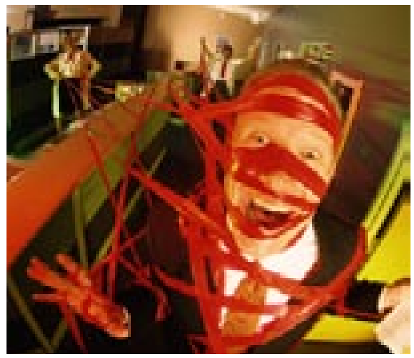



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